

The a2 Milk Company™



Half yearly report
for the six months ended
31 December 2015



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Chairman's Letter

Dear Shareholder,

I am pleased to report on the continuing progress of The a2 Milk Company Limited ("a2MC" or the "Company") during the six months to 31 December 2015.

The Company and its subsidiaries (together the "Group") achieved Group revenue of \$139.1 million and Group profit after tax of \$10.1 million. This is an exceptional result for the half and reflects the significant contribution from the Australian and New Zealand (ANZ) segment, strong profitable growth out of our China business, and the continued investment in our strategic growth initiatives in the USA and UK. The balance sheet remained strong with nil debt and cash on hand at balance date of \$36.4 million.

On 8 October 2015, the Company announced its intention to raise \$40 million of new equity through a fully-underwritten placement of fully paid new ordinary shares in the Company, and a further \$3 million through a Share Purchase Plan (SPP). The placement and SPP were successfully completed 9 October 2015 and 26 November 2015 respectively. The Board was delighted with the level of support the Company received throughout the process and believe the Company is now well resourced to execute on opportunities consistent with our strategic agenda.

For some time the Board has indicated that it is looking to appoint additional independent directors. We are therefore delighted to announce the appointment of Mr Peter Hinton

as an Independent Non-Executive Director of the Company with effect from 16 February 2016. Mr Hinton is a partner at the law firm Simpson Grierson in New Zealand and is a highly regarded commercial lawyer with substantial experience in this market and international markets. Mr Hinton has provided legal advice to the Company over many years and this background together with his very strong commercial skills is highly relevant and complementary to the make-up of the Board. This is particularly so given the increasing complexity of the business and the breadth of activities in international markets.

The Board will continue its process of renewal with the appointment of an additional director with appropriate international skills and experience planned during this calendar year.

The Managing Director's report contains further detail on the Group's operational performance.

I wish to thank our Management, Staff and my fellow Directors for their significant efforts and also our customers, business partners and shareholders for their continued support.



David Hearn
Chairman & Executive Director
16 February 2016

CEO's Report

Overview

The a2 Milk Company ("a2MC" or the "Company") has delivered an outstanding result for the first half of the financial year to 31 December 2015, notwithstanding higher investment in our growth markets of \$8.1 million. The Australia and New Zealand (ANZ) business continues to outperform with substantial growth in revenue and operating earnings as a consequence of exceptional growth in a2 Platinum® infant formula. The China and Other Asia business also recorded significant growth in revenue from infant formula and for the first time returned positive operating earnings. Growth initiatives in the USA focused on establishing broad distribution of a2 Milk™ in the state of California and in the UK our fresh milk business showed improvement following its repositioning into the specialty milk segment.

The unaudited Group profit after tax for the 6 months ended 31 December 2015 was \$10.1 million and included:

- Total revenue of \$139.1 million, an increase of 86% over the prior corresponding period (pcp)
- Group operating EBITDA¹ of \$18.7 million, representing a 472%² increase on pcp. The result includes expensing establishment costs in the USA and UK markets of \$8.1 million, record operating performance in ANZ and significant growth in China
- EBITDA before inter-company charges³ for the ANZ operations of \$34.5 million, an increase of 146% on the pcp

- EBITDA before inter-company charges for China and other Asia totalling \$1.2 million
- EBITDA before inter-company charges for UK and USA totalling (\$8.1) million
- Corporate and other costs before inter-company charges of \$8.9 million
- Group income tax charge of \$7.4 million⁴
- Basic earnings per share (EPS) of 1.52¢; and diluted EPS of 1.50¢

The increase in corporate and other costs in the half is primarily a result of higher employee share scheme expenses, increased research and development costs associated with a higher level of activity and legal expenses.

Cash on hand at half year end was \$36.4 million, reflecting positive cash inflows from equity raising activities, partially offset by an investment in working capital to fund the significant growth in infant formula. We are forecasting a significantly improved operating cash flow for the second half.

Other Corporate Initiatives

The Company undertook an equity raising in October 2015 comprising a placement to institutional investors and shareholders to raise NZ\$40 million and a Share Purchase Plan to raise a further NZ\$3 million, both of which were

¹ Earnings before interest, tax, depreciation and amortisation (EBITDA) is a non GAAP measure. However, the Company believes that it provides investors with a comprehensive understanding of the underlying performance of the business. A reconciliation of EBITDA to net profit after tax is provided at the end of the CEO report

² Before non-recurring items in 1H15 of \$0.8 million relating to ASX listing costs

³ Inter-company charges include licence fees payable to the Parent, and marketing and herd testing costs payable by the Parent

⁴ The high income tax charge represents non-deductible expenses largely related to the Company's employee share scheme and international losses not fully tax effected

CEO's report cont.

For the six months ended 31 December 2015

substantially oversubscribed. This raising was undertaken primarily to fund the increase in working capital associated with the significant growth in infant formula sales and to maintain the conservative approach to managing the Company's capital position.

The decision to gain admission to the Official List of the Australian Securities Exchange (ASX) in March 2015 has achieved the key objective of broadening investor participation alongside the existing NZX Main Board listing. As at 10 February 2016, the number of Australian investors has increased to over 22,000, representing ~64% of shares on issue.

Strategic Agenda Update

The Company continues to execute on its strategy of growing the ANZ and China businesses and developing growth opportunities in the UK and USA markets.

As recently indicated, infant formula has emerged as a significant contributor to growth and earnings for the Group as a whole. The Company has also identified a significant growth opportunity in a2 Milk™ branded milk powder which was launched in limited release from June 2015. For the first half period to 31 December 2015, revenue from infant formula in ANZ and China grew to NZ\$73.9 million, representing an increase of 340% on the pcp and accounted for 53% of total Group turnover. The majority of sales occurred within the Australian grocery and pharmacy channels. In addition, direct sales into China increased significantly with strong growth in the cross border e-commerce channels and mother & baby retail stores (MBS).

Our infant formula business in both ANZ and China is being well supported by our manufacturing partner in New Zealand, Synlait Milk Limited. We experienced stock shortages, in particular during the first four months of the half. However we have increased our production schedule with Synlait to meet increased demand. The Company is in the process of further building milk supply in New Zealand to facilitate further increases in infant formula production during FY17.

The infant formula regulatory environment in China continues to evolve however the Company considers itself well placed to respond to changes in regulation in conjunction with its manufacturing partner.

ANZ

The ANZ business continued to perform extremely well, with sales growth and operating earnings in Australia

substantially ahead of budget and the corresponding period last year. Total revenue in AUD across all product categories increased by 77% on pcp to \$117.5 million, and Operating EBITDA before intercompany charges totalled \$34.5 million (an increase of 146% on pcp).

Fresh milk sales of a2 Milk™ continue to grow and recorded an increase on the pcp of 5% in AUD. A new creative advertising campaign, "Believe in better", was launched in October across a number of advertising platforms and is assisting in further building brand awareness and scale. This positioning is being rolled out across other product categories in Australia. Market share of a2 Milk™ fresh milk in Australia by value has remained stable at approximately 9.3% (Australian Grocery Weighted Scan 20 December 2015 MAT).

Sales of a2 Platinum® infant formula in both grocery and pharmacy channels in Australia showed exceptional growth, in particular in the months of November and December when increased levels of finished product were received and delivered to customers. As previously advised, the Company has been progressively increasing the size of its production orders from its supplier to match the continually increasing demand. However retailers continue to experience out of stocks on shelf and we have yet to build a meaningful level of inventory on hand.

a2 Platinum® has been the fastest growing infant formula brand in the Australian market in the last four quarterly periods. The brand achieved a 16.7% grocery/pharmacy scan market share for the 13 weeks ending 20 December 2015 by value with two products ranked in the category's top five.

The Company has commented previously on its plans to broaden the product portfolio in Australia beyond liquid milk and Infant Formula. a2 Milk™ whole milk powder was launched in June 2015 and sales are building in this market and into China, albeit limited in the short term by supply constraints. a2 Ice Cream™ was launched in two major retailers from August, and distribution has been broadened into a third major retailer from January 2016.

China

Following a number of years of establishment and investment, the China business performed well ahead of plan, and returned a positive EBITDA for the first time.

The new arrangements whereby a2MC assumed responsibility for direct sales and distribution together with an expansion of our local Shanghai team have been

CEO's report cont.

For the six months ended 31 December 2015

positive for the business. We have implemented a multi-product, multi-channel strategy to achieve growth in both China label and cross-border ANZ label infant formula, with a strong focus on e-commerce channels and MBS. We also commenced building sales in a2 Milk™ branded whole milk powder. Our Shanghai based team has been broadened beyond marketing and health care professional capabilities to include sales management and e-commerce.

The Company's China e-commerce strategy is centred on building multiple strong relationships with profile providers such as Tmall and JD.com (China's largest online direct sales platform), and a number of other strategic platforms. Our participation in the November "11/11" key annual sales event was considered by our main partners to be very successful. Tmall data showed sales from The a2 Milk Company™ flagship store were in the top three cross border infant formula brands. We are confident that these relationships will deliver increasing sales and assist with consumer education around the A2 protein proposition.

With our new sales management capability we have increased our bricks and mortar distribution network to over a thousand MBS stores served by 32 distributors, with particular strength in East and West China and with further growth planned in the second half. To assist building this network, a2 Platinum® was showcased at the annual Children Baby Mother Expo (CBME) in Shanghai in July 2015. In October we entered into an exclusive distributor agreement for five key provinces in China with DKSH (China) Co., Ltd, a well credentialed distributor in key Asian markets.

UK

The UK business is on track to achieve monthly breakeven by year end, owing to the revised business model involving the repositioning of our fresh milk offering into the premium specialty milk segment, along with a broadening of the product portfolio. We continue to explore opportunities to more quickly build scale in this relatively small business.

We are pleased with the support from our customers with ranging in four of the top five retailers. Distribution grew to around 1,200 stores during the half and our selling team is highly focused on building rate of sale in each customer account. We have developed improved point of sale presence and digital marketing executions, undertaken targeted promotional events and we continue to build relationships and activities with the health care

professional community. A new advertising and shopper marketing campaign is to be run during the second half with a focus on the unique benefits of a2 Milk™ products.

The plan to extend the product portfolio is progressing positively with UHT long life milk launched from September in selected channels and the commencement of a trial for a2 Platinum® infant formula. The Company continues to be well supported by our fresh milk supply partner, our newly appointed UHT contract packer and our committed local farmers.

USA

Our plan for the USA liquid milk market has involved a launch of a2 Milk™ into the West Coast region and the achievement of agreed milestones prior to extending distribution into further state markets. Our launch into Southern California commenced from April 2015 and extended into Northern California from September. The product is positioned in the specialty milk section, which remains the fastest growing segment of the total milk category and our product is available in four variants.

We are pleased with the progress achieved in building retail distribution in California during the half. Whilst the rate of growth in store numbers and therefore sales performance has been a slower build than we originally targeted, we have now achieved broad trade acceptance and our retail weighted distribution has been progressively building. Our sales focus has been and will continue to be in building unit sales per store per week (UPSW) relevant to the speciality milk category and we are on track to deliver the target of 30 UPSW for the range, by the end of FY16. Following presentations to the final remaining major retailer group in California during December, we should achieve retail weighted distribution across the state of over 85% during February. This retail coverage is ahead of our original plan.

In parallel with building retail distribution we have been further developing our launch marketing and communication activities. This has included digital and social media platforms and activities, establishing promotional programs with retailers and a public relations program. We are to commence our first television advertising campaign focused on the Los Angeles market beginning mid-February. The TV campaign will be across both broadcast and cable TV networks and be supported by a social, digital, and shopper marketing campaign which will extend across all of California given the increased level of distribution in place by that time.

CEO's report cont.

For the six months ended 31 December 2015

We have successfully established our milk sourcing, processing and logistics supply chain to service California, with ready capability to extend into further markets. Our farmer base is currently in Nebraska and the North-East and we have initiated a best practice on-farm management program with our suppliers. In addition, we have been very pleased with the operational support received from our contract processor Byrne Dairy during this establishment phase.

While we are still at an early stage of development, our monthly sales performance continues to build and feedback from both consumers and customers is positive and encouraging. Given the build in retail distribution, the Board has agreed additional marketing spend above the original budget of US\$3 million during the second half.

Research and Development (R&D) and Intellectual Property (IP)

The Company continues to enhance and extend the scope of its brand assets, further develop its comprehensive IP portfolio and participate in R&D programs characterising the benefits of the A2 beta casein protein ("A2 protein") and absence of the A1 beta casein protein ("A1 protein").

Research published during the first half demonstrates the mechanisms underpinning the digestive benefits of A1 protein free milk products on human health. This published work is complemented by a second completed human clinical trial in China that supports the digestive advantages of a2 Milk™, which has been submitted for publication.

The Company has commissioned two additional human clinical trials – the first will be led by Professor Peter Gibson in association with Monash University, Australia. The second will be with a leading biomedical research centre in the USA. Further clinical trials to assess the benefits in adults, pre-schoolers, and infants have also commenced in China.

In December 2015, the New Zealand Government awarded the Company a NZ\$1.1 million research grant in partnership with AgResearch and The University of Auckland to validate the digestive benefits of A2 beta casein protein. The three year grant was one of seven grants issued as part of a government push to invest funds into areas of High-Value Nutrition.

The Company's action against the Australian Broadcasting Corporation for misleading and deceptive conduct was successfully settled in the Federal Court in November.



Geoffrey Babidge
Managing Director & Chief Executive Officer
16 February 2016

CEO's report cont.

For the six months ended 31 December 2015

Reconciliation of EBITDA to net profit after tax (NPAT)

	Half year ended 31 Dec 15 NZ \$000's	Half year ended 31 Dec 14 NZ \$000's	Movement %
			
EBITDA	18,683	2,504	646%
EBITDA before non-recurring items	18,683	3,266	472%
Depreciation/amortisation	(1,255)	(912)	38%
EBIT before non-recurring items	17,428	2,354	640%
Non-recurring items ⁵	–	(762)	
Interest income	142	88	61%
Interest expense	(38)	–	
Income tax/(expense)	(7,425)	(1,555)	377%
Net profit after tax (NPAT)	10,107	125	7,986%

⁵Non-recurring items in 2015 relate to costs associated with the Company's listing on the ASX

Directors' declaration

For the six months ended 31 December 2015

The Directors of The a2 Milk Company Limited are pleased to present the half yearly report for the six months ended 31 December 2015.

The report presented is signed for and on behalf of the board and was authorised for issue on 16 February 2016.

The half yearly report is unaudited.



David Hearn
Chairman & Executive Director
16 February 2016



Geoffrey Babidge
Managing Director & Chief Executive Officer

Auditor's review report

For the six months ended 31 December 2015



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Review Report to the Shareholders of The a2 Milk Company Limited ("the company") and its subsidiaries together ("the group")

We have reviewed the interim financial statements on pages 10 to 19, which comprise the statement of financial position as at 31 December 2015, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the period ended on that date, and a summary of significant accounting policies and other explanatory information.

This report is made solely to the company's shareholders, as a body, in accordance with our engagement letter. Our review has been undertaken so that we might state to the company's shareholders those matters we are required to state to them in a review report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's shareholders as a body, for our review work, for this report, or for our findings.

Directors' Responsibilities

The directors are responsible for the preparation and fair presentation of interim financial statements which comply with generally accepted accounting practice in New Zealand as it relates to interim financial statements and for such internal control as the directors determine is necessary to enable the preparation and fair presentation of the interim financial statements that are free from material misstatement, whether due to fraud or error.

Reviewer's Responsibilities

Our responsibility is to express a conclusion on the interim financial statements based on our review. We conducted our review in accordance with NZ SRE 2410 Review of Financial Statements Performed by the Independent Auditor of the Entity. NZ SRE 2410 requires us to conclude whether anything has come to our attention that causes us to believe that the financial statements, taken as a whole, are not prepared in all material respects, in accordance with generally accepted accounting practice in New Zealand as it relates to interim financial statements. As the auditor of The a2 Milk Company Limited, NZ SRE 2410 requires that we comply with the ethical requirements relevant to the audit of the annual financial statements.

Basis of Statement

A review of interim financial statements in accordance with NZ SRE 2410 is a limited assurance engagement. The auditor performs procedures, primarily consisting of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures.

The procedures performed in a review are substantially less than those performed in an audit conducted in accordance with International Standards on Auditing (New Zealand). Accordingly we do not express an audit opinion on those financial statements.

Other than in our capacity as assurance practitioner we have no relationship with, or interests in, the group.

Conclusion

Based on our review nothing has come to our attention that causes us to believe that the accompanying interim financial statements, set out on pages 10 to 19, do not present fairly, in all material respects, the financial position of the group as at 31 December 2015 and its financial performance and cash flows for the six month period ended on that date in accordance with generally accepted accounting practice in New Zealand as it relates to interim financial statements.

Our review was completed on 16 February 2016 and our findings are expressed as at that date.

Ernst & Young
Sydney

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Condensed consolidated statement of comprehensive income

For the Six Months Ended 31 December 2015

	Notes	6 Months 31 Dec 15 (Unaudited) \$'000	6 Months 31 Dec 14 (Unaudited) \$'000
CONTINUING OPERATIONS			
Sales		139,090	74,659
Cost of sales		(82,090)	(48,543)
Gross Margin		57,000	26,116
Interest income		142	88
Other revenue		136	126
Administrative expenses	3	(13,260)	(6,770)
Finance costs		(123)	(41)
Marketing expenses	4	(10,044)	(6,886)
Occupancy expenses		(309)	(263)
Other expenses	5	(16,010)	(10,690)
Profit before tax		17,532	1,680
Income tax expense		(7,425)	(1,555)
PROFIT AFTER TAX FOR THE PERIOD		10,107	125
Items of other comprehensive income that may be reclassified to profit or loss:			
Foreign currency translation loss	6	(1,999)	(1,545)
TOTAL COMPREHENSIVE INCOME/(LOSS)		8,108	(1,420)
Earnings per share			
Basic (cents per share)		1.52	0.02
Diluted (cents per share)		1.50	0.02

The accompanying notes form part of these financial statements.

Condensed consolidated statement of changes in equity

For the Six Months Ended 31 December 2015

	Notes	6 Months 31 Dec 15 (Unaudited) \$'000	6 Months 31 Dec 14 (Unaudited) \$'000
Equity at the beginning of period.....		58,629	58,644
Total comprehensive income/(loss) for the period		8,108	(1,420)
		<u>66,737</u>	<u>57,224</u>
TRANSACTIONS WITH OWNERS			
Employee equity settled payments reserve		1,439	419
Issue of ordinary shares	7	43,750	–
Share issue costs.....	7	(2,149)	–
EQUITY AT END OF THE PERIOD		<u>109,777</u>	<u>57,643</u>
EQUITY COMPRISES:			
Share capital			
Balance at beginning of period		86,303	86,264
Issue of ordinary shares		43,750	–
Share issue costs.....		(2,149)	–
Balance at end of period		<u>127,904</u>	<u>86,264</u>
Retained earnings/(deficit)			
Balance at beginning of period		(26,065)	(23,974)
Net surplus for the period		10,107	125
Balance at end of period		<u>(15,958)</u>	<u>(23,849)</u>
Foreign currency translation reserve			
Balance at beginning of period		(5,711)	(6,665)
Movements during the period		(1,999)	(1,545)
Balance at end of period		<u>(7,710)</u>	<u>(8,210)</u>
Employee equity settled payments reserve			
Balance at beginning of period		4,102	3,019
Movements during the period		1,439	419
Balance at end of period		<u>5,541</u>	<u>3,438</u>
EQUITY AT END OF THE PERIOD		<u>109,777</u>	<u>57,643</u>

The accompanying notes form part of these financial statements.

Condensed consolidated statement of financial position

As at 31 December 2015

	Notes	As at 31 Dec 15 (Unaudited) \$'000	As at 30 June 15 (Audited) \$'000
ASSETS			
Current assets			
Cash & short term deposits		36,426	6,092
Trade and other receivables.....		65,458	39,944
Prepayments.....	9	26,488	9,651
Inventories.....	9	16,091	4,846
Total current assets		144,463	60,533
Non-current assets			
Property, plant & equipment		8,812	9,301
Goodwill.....		10,517	10,993
Other intangible assets		5,881	6,230
Deferred tax asset		2,793	1,810
Total non-current assets		28,003	28,334
TOTAL ASSETS		172,466	88,867
LIABILITIES			
Current liabilities			
Trade and other payables.....		57,409	28,357
Current tax liabilities		5,060	595
Total current liabilities		62,469	28,952
Non-current liabilities			
Accounts payable.....		220	189
Deferred tax liability		–	1,097
Total non-current liabilities		220	1,286
TOTAL LIABILITIES		62,689	30,238
EQUITY			
Equity attributable to equity holders of the parent			
Share capital		127,904	86,303
Retained earnings/(deficit)		(15,958)	(26,065)
Foreign currency translation reserve.....		(7,710)	(5,711)
Employee equity settled payments reserve		5,541	4,102
TOTAL EQUITY		109,777	58,629
TOTAL LIABILITIES & EQUITY		172,466	88,867

The accompanying notes form part of these financial statements.

Condensed consolidated statement of cash flows

For the six months ended 31 December 2015

	6 Months 31 Dec 15 (Unaudited) \$'000	6 Months 31 Dec 14 (Unaudited) \$'000
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash was provided from (applied to):		
Receipts from customers.....	115,878	71,413
Interest received.....	142	88
Interest paid.....	(38)	–
Other income.....	136	126
Payments to suppliers & employees.....	(117,629)	(71,967)
Taxes paid.....	(8,450)	(3,767)
Net cash inflow/(outflow) from operating activities	(9,961)	(4,107)
CASH FLOWS FROM INVESTING ACTIVITIES		
Cash was provided from (applied to):		
Payment for property, plant & equipment.....	(603)	(266)
Investment in other intangible assets.....	(441)	(1,895)
Net cash outflow from investing activities	(1,044)	(2,161)
CASH FLOWS FROM FINANCING ACTIVITIES		
Cash was provided from (applied to):		
Proceeds from issue of equity shares.....	43,750	–
Payment for capital raising costs.....	(2,149)	–
Net cash inflow from financing activities	41,601	–
Net increase/(decrease) in cash & short term deposits.....	30,596	(6,268)
Cash & short term deposits at the beginning of the period.....	6,092	15,979
Effect of exchange rate changes on cash.....	(262)	152
Cash and short term deposits at the end of the period	36,426	9,863
COMPRISED OF:		
Cash & short term deposits	36,426	9,863

The accompanying notes form part of these financial statements.

Notes to the condensed consolidated financial statements

For the six months ended 31 December 2015

1. STATEMENT OF COMPLIANCE

The a2 Milk Company Limited (the “Company”) is a profit-oriented entity incorporated and domiciled in New Zealand. The registered office is located at c/o Simpson Grierson, Level 27, 88 Shortland Street, Auckland, New Zealand.

The principal activity of the Company and its subsidiaries (together the “Group”) is the commercialisation of the a2 Milk™ brand and related products as supported by the ownership of intellectual property that enables the identification of cattle for the production of a2 Milk™. The Company sources and supplies the a2 Milk™ brand milk in Australia

through its 100% owned subsidiary The a2 Milk Company (Australia) Pty Limited, in the UK through its 100% owned subsidiary The a2 Milk Company Limited (UK), and in the USA through its 100% owned subsidiary The a2 Milk Company Limited (USA). The Company supplies a2 Platinum® brand infant formula through its 100% owned subsidiaries A2 Infant Nutrition Limited (New Zealand), A2 Infant Nutrition Australia Pty Limited (Australia) and The a2 Milk Company Limited (UK).

The a2 Milk Company Limited is registered in New Zealand under the Companies Act 1993. The Company is a FMC reporting entity for the

purposes of Part 7 of the Financial Markets Conduct Act 2013 and its financial statements comply with that Act and the Companies Act 1993. The shares of the Company are publicly traded on the NZX Main Board and the Australian Securities Exchange (ASX).

The unaudited half year report has been prepared in accordance with New Zealand equivalent to International Accounting Standard 34 (NZ IAS-34) *Interim Financial Reporting*. The half year report should be used in conjunction with the Group’s annual report for the 12 months ended 30 June 2015.

The following Standards and Interpretations were effective for the first time in the current period

Pronouncement

Effective for periods beginning

Fair Value Disclosures by Retirement Benefit Plans - Amendments to NZ IAS 26
2014 Omnibus Amendments to NZ IFRS (NZ IFRS 1, IFRS 44, NZ IFRS 4, NZ IFRS 7)

1 January 2015
1 July 2015

The above Standards and Interpretations have not led to any changes in the Company’s accounting policies, and have no measurement or recognition impact on the periods presented in this half year report.

At period end date, a number of Standards and Interpretations were in issue but not yet effective. The Group is yet to assess the full impact of these standards. However, the standards are unlikely to have a significant effect on the Group’s financial statements.

Notes to the condensed consolidated financial statements cont.

 For the six months ended 31 December 2015

2. BASIS OF PREPARATION

The financial statements have been prepared on the basis of historical cost. Cost is based on the fair values of the consideration given in exchange for assets.

Accounting policies are selected and applied in a manner which ensures that the resulting financial information satisfies the concepts of relevance and reliability, thereby ensuring that the substance of the underlying transactions or other events is reported.

The financial statements are presented in New Zealand dollars.

The same accounting policies and methods of computation are followed in this half year report as were applied in the preparation of the Group's financial statements for the year ended 30 June 2015.

3. ADMINISTRATIVE EXPENSES

	6 Months 31 Dec 15 (Unaudited) \$'000	6 Months 31 Dec 14 (Unaudited) \$'000
Employee equity compensation	1,439	419
Salary & wage costs	8,162	4,439
Other administrative expenses.....	3,659	1,912
	<u>13,260</u>	<u>6,770</u>

The increase in salary & wage costs includes headcount increases associated with the growth of the business, including the USA following the launch in April 2015. Other expenses include increased travel costs of \$1,123,000 pertaining to increased activity in international markets.

4. MARKETING EXPENSES

Marketing expenses have increased compared to the prior corresponding period by \$3,158,000 primarily in relation to growth initiatives in the UK and USA, and China and other Asia segments.

5. OTHER EXPENSES

	6 Months 31 Dec 15 (Unaudited) \$'000	6 Months 31 Dec 14 (Unaudited) \$'000
Freight.....	6,631	4,655
Consultancy, accounting & secretarial fee.....	3,156	1,711
Legal expenses.....	1,352	441
Depreciation & amortisation.....	1,255	912
Patents, trademarks and research & development	1,023	207
Other operating expenses	2,593	2,002
Non-recurring items – Australian Securities Exchange (ASX) dual listing.....	–	762
	<u>16,010</u>	<u>10,690</u>

Legal expenses include costs associated with the documentation of new arrangements in China and costs associated with an expression of interest.

Non-recurring items represent costs associated with the ASX dual listing process during the six months to 31 December 2014.

Notes to the condensed consolidated financial statements cont.

 For the six months ended 31 December 2015

6. FOREIGN CURRENCY TRANSLATION LOSS

The foreign currency translation loss in the six months to 31 December 2015 has primarily arisen on the translation of Australian dollar advances to subsidiary companies which have been negatively impacted by the strengthening of the New Zealand Dollar during the period.

7. SHARE CAPITAL

	As at 31 Dec 15 (Unaudited) \$'000	As at 30 June 15 (Audited) \$'000
a) Share capital		
Balance at beginning of period.....	86,303	86,264
Ordinary Shares: Partly paid shares fully paid.....	750	39
Ordinary shares: Underwritten Placement.....	40,000	–
Ordinary shares: Share Purchase Plan	3,000	–
	<u>130,053</u>	<u>86,303</u>
Less: Capital raising costs	(2,149)	–
Balance at end of period	<u>127,904</u>	<u>86,303</u>
	31 Dec 15 (Unaudited) No.	30 June 15 (Audited) No.
b) Number of ordinary shares on issue		
(i) Fully paid ordinary shares		
Balance at beginning of period.....	633,326,979	633,066,979
Shares issued.....	70,233,086	260,000
Balance at end of period	<u>703,560,065</u>	<u>633,326,979</u>
(ii) Partly paid ordinary shares		
Balance at beginning of period.....	26,740,000	27,000,000
Shares fully paid	(7,000,000)	(260,000)
Balance at end of period	<u>19,740,000</u>	<u>26,740,000</u>
(iii) Total shares on issue		
Fully paid ordinary shares.....	703,560,065	633,326,979
Partly paid ordinary shares.....	19,740,000	26,740,000
Balance at end of period	<u>723,300,065</u>	<u>660,066,979</u>

Partly paid ordinary shares carry the same rights and entitlements on a fractional basis, as fully paid ordinary shares, with such fractions being equivalent to the proportion which the amount paid is of the total amount paid and amounts still payable on the shares.

Issue of Shares

During the period, issued share capital was increased by \$41,601,000. This comprised the issue of 58,823,529 fully paid ordinary shares by way of share placement; 4,409,557 fully paid ordinary shares by way of a Share Purchase Plan; and 7,000,000 partly paid shares that were fully paid during the period.

Notes to the condensed consolidated financial statements cont.

For the six months ended 31 December 2015

8. OPERATING SEGMENT INFORMATION

The Group has adopted NZ IFRS-8 *Operating Segments*. NZ IFRS-8 requires operating segments to be identified on the basis of internal reports about components of the Company that are regularly reviewed by the chief operating decision maker in order to allocate resources to the segment and assess its performance.

For management purposes, the Group is organised into business units based on geographical location along with a corporate function, and has four reportable operating segments as follows:

- The *Australia and New Zealand* segment receives revenue from milk, cream, infant formula, whole milk powder and ice cream sales, and royalty and licence fee income
- The *China and other Asia* segment receives revenue from milk, infant formula and whole milk powder sales. This segment is responsible for the infant formula supply chain originating from New Zealand
- The *United Kingdom and USA* segment receives revenue from milk and infant formula sales
- The *Corporate* and other segment revenue comprises external royalty and licence fee income. Corporate and other segment profit also includes:
 - internal royalty, licence fee and management fee income from subsidiaries; and
 - costs, such as marketing and herd testing costs, associated with development of intellectual property globally

Management monitors the operating results of its business units separately for the purpose of making decisions about resource allocation and performance assessment. Segment performance is evaluated based on operating profit or loss and is measured consistently with operating profit or loss in the consolidated financial statements.

Transfer prices between operating segments are on an arm's length basis in a manner similar to transactions with third parties.

	Segment Revenue		Segment EBITDA	
	6 Months 31 Dec 15 (Unaudited) \$'000	6 Months 31 Dec 14 (Unaudited) \$'000	6 Months 31 Dec 15 (Unaudited) \$'000	6 Months 31 Dec 14 (Unaudited) \$'000
CONTINUING OPERATIONS				
Australia and New Zealand	127,910	72,794	9,262	4,876
China and other Asia	8,400	1,076	1,015	(610)
UK and USA ⁶	2,887	892	(5,543)	(1,919)
Corporate and other	29	23	13,949	157
Segment revenue & EBITDA ⁷	139,226	74,785	18,683	2,504
Net Interest income			104	88
Depreciation and amortisation			(1,255)	(912)
Income tax income/(expense)			(7,425)	(1,555)
CONSOLIDATED SEGMENT PROFIT			10,107	125

Over 56% of sales come from three customers in Australia (2014: over 68% from three customers).

⁶The Company launched in the USA during the second quarter of calendar 2015 and therefore there is no revenue from the USA included in the UK and USA Segment for the period ended 31 December 2014

⁷EBITDA is a non-GAAP measure and represents earnings before interest, taxation, depreciation and amortisation

Notes to the condensed consolidated financial statements cont.

For the six months ended 31 December 2015

8. OPERATING SEGMENT INFORMATION cont.

	Depreciation & Amortisation		Additions to Non-Current Assets	
	6 Months	6 Months	6 Months	6 Months
	31 Dec 15	31 Dec 14	31 Dec 15	31 Dec 14
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)
	\$'000	\$'000	\$'000	\$'000
Australia and New Zealand	539	566	605	48
China and other Asia	207	195	204	–
UK and USA	397	32	54	1,712
Corporate and other	112	119	181	401
	<u>1,255</u>	<u>912</u>	<u>1,044</u>	<u>2,161</u>

	Assets		Liabilities	
	31 Dec 15	30 June 15	31 Dec 15	30 June 15
	(Unaudited)	(Audited)	(Unaudited)	(Audited)
	\$'000	\$'000	\$'000	\$'000
Australia and New Zealand	69,349	47,969	24,028	14,691
China and other Asia	57,905	18,372	30,209	8,522
UK and USA	7,376	6,412	3,393	3,818
Corporate and other	37,836	16,114	5,059	3,207
	<u>172,466</u>	<u>88,867</u>	<u>62,689</u>	<u>30,238</u>

Additions to Non-Current Assets include additions to property, plant and equipment, and other intangibles.

Notes to the condensed consolidated financial statements cont.

 For the six months ended 31 December 2015

**9. RECONCILIATION OF NET SURPLUS AFTER TAXATION
 WITH NET CASH FLOWS FROM OPERATING ACTIVITIES**

	6 Months 31 Dec 15 (Unaudited) \$'000	6 Months 31 Dec 14 (Unaudited) \$'000
Net surplus for the year.....	10,107	125
Adjustments for non-cash items:		
Depreciation & amortisation expense.....	1,255	912
Loss on disposal	–	16
Expense recognised in profit & loss in respect of equity-settled share-based payments.....	1,439	419
Net foreign exchange (gain)/loss	(634)	(1,174)
Deferred tax	(2,080)	(32)
	<u>10,087</u>	<u>266</u>
Movements in working capital		
Increase in trade and other receivables.....	(25,514)	(3,322)
Increase in prepayments.....	(16,837)	(2,265)
Increase in inventories	(11,245)	(2,543)
Increase in trade and other payables.....	29,083	5,166
Increase/(decrease) in current tax liabilities.....	4,465	(1,409)
Net cash outflow from operating activities	<u>(9,961)</u>	<u>(4,107)</u>

Increases in prepayments and inventories are predominantly attributable to the acquisition of infant formula during the period.

10. NET TANGIBLE ASSETS PER SECURITY

	As at 31 Dec 15 (Unaudited) \$...	As at 31 Dec 14 (Unaudited) \$...
Net tangible assets per security	0.13	0.06

Corporate directory

Company	The a2 Milk Company Limited c/o Simpson Grierson Level 27 88 Shortland Street Auckland 1010 New Zealand	Financial Advisor	Goldman Sachs New Zealand Limited Level 39 Vero Centre 48 Shortland Street Auckland 1010 New Zealand
New Zealand Share Registry	Link Market Services Limited PO Box 91976 Victoria Street West Auckland 1142 New Zealand Telephone: +64 9 375 5998	Auditor	Ernst & Young 680 George Street Sydney NSW 2000 Australia
Australian Share Registry	Link Market Services Limited Locked Bag A14 Sydney South NSW 1235 Australia Telephone: +61 1300 554 474	Registered office	c/o Simpson Grierson Level 27 88 Shortland Street Auckland 1010 New Zealand Level 11 80 Mount Street North Sydney NSW 2060 Australia Telephone: +61 2 9697 7000
Legal Advisors	Simpson Grierson Level 27 88 Shortland Street Auckland 1010 New Zealand DLA Piper Level 22 1 Martin Place Sydney NSW 2000 Australia	Corporate website	www.thea2milkcompany.com
Company Directors	David Hearn (Chairman & Executive Director) Julia Hoare (Deputy Chairman & Non-Executive Director) Geoffrey Babidge (Managing Director & Chief Executive Officer) Richard Le Grice (Non-Executive Director) Melvyn Miles (Non-Executive Director)		





The
a2 Milk
Company